

## IRS Issues Debit/Credit Card Ruling

On May 6, 2003, the Internal Revenue Service released Revenue Ruling 2003-43. This Revenue Ruling addresses the issue of whether employer-provided expense reimbursements made through debit or credit cards and other electronic media are excludable from gross income. While the issue is broad and applies to all health plans, the specifics of the Revenue Ruling only address health flexible spending accounts (FSAs) and Health Reimbursement Arrangements (HRAs).

The Revenue Ruling describes three situations, and then renders an opinion as to whether or not each situation complies with the claim substantiation requirements. Two of the situations are virtually identical; the difference being that one involves a debit card and the other involves a credit card. The IRS determined that these situations were such that expense reimbursements would be excluded from gross income.

The following facts applied in these situations:

- Each participating employee certifies upon enrollment and each year thereafter that the card will only be used for eligible medical care expenses as defined in Internal Revenue Code Section 213(d) for the employee, spouse or dependents.
- Each employee also certifies that any expense paid with the card has not been reimbursed and that the employee will not seek reimbursement under any other plan covering health benefits.
- These certifications are printed on the back of the card and employees reaffirm the certification each time the card is used.
- The cardholder also agrees to acquire and retain sufficient documentation for any expense paid with the card, including invoices and receipts, where appropriate.
- The card is automatically cancelled at termination of employment.
- The cardholder's use of the card is limited to the maximum dollar amount of coverage available in the cardholder's health FSA or HRA.
- The employer limits the card's use to specified merchant codes relating to health care—physicians, pharmacists, dentists, vision care offices, hospitals and other medical care providers.

To provide assurance that only eligible medical expenses are reimbursed, the employer establishes the following procedures:

If the dollar amount of the transaction at a health care provider equals the dollar amount of the copayment for that service under the plan, the charge is considered fully substantiated without the need for the employee to submit a receipt for further review.

- The employer permits automatic reimbursement without further review of recurring expenses that match expenses previously approved as to amount, provider and time period, such as for an employee who refills a prescription on a regular basis.
- If the merchant, provider or other party, such as a Pharmacy Benefit Manager, verifies at the time of sale that the charge is for a medical expense, the charge is considered fully substantiated.
- The employer's procedures provide that all other charges are treated as conditional pending confirmation of the charge. The employer requires receipts for such expenses that include a description of the service or product, the date of the service or sale and the amount.
- An employee may also obtain benefits without the use of the card by submitting a claim.

Furthermore, the employer adopts the correction procedures with respect to improper payments.

The Revenue Ruling also describes a situation that does not meet the claim substantiation requirements. In this situation, the employer does not review any transactions below a certain dollar threshold or that is a multiple of a specified whole dollar amount, such as a copayment. The employer applies sampling techniques to other claims and only those selected as part of the sample must be substantiated. The IRS said that the sampling technique described does not meet the requirements, but asked for comments about other sampling techniques that might be satisfactory. The IRS went on to point out that failure to meet the claim substantiation requirement means that all reimbursements under the plan are taxable.

The IRS also pointed out that the 1099 requirements apply to payments made through debit, credit or stored-value cards. These requirements apply if a plan pays a provider \$600 or more in a year. Currently, debit and credit card technology does not give employers access to the tax ID numbers of healthcare providers who accept debit or credit cards, making it impractical for the 1099 requirement to apply.

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